

BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 2018-82-S

IN RE:)
)
 Application of Palmetto Wastewater Reclamation,)
 LLC for adjustment of rates and charges)
 and for modifications to certain terms and)
 conditions for the provision of sewer)
 service.)
 _____)

PREFILED DIRECT TESTIMONY OF MARK S. DADAY
ON BEHALF OF PALMETTO WASTEWATER RECLAMATION LLC

Q. PLEASE STATE YOUR NAME, PRESENT POSITION, AND BUSINESS ADDRESS.

A. My name is Mark S. Daday. I am employed as the President of Ni Pacolet Milliken Utilities, LLC (“Ni”) and all of its direct and indirect subsidiaries, which includes the applicant, Palmetto Wastewater Reclamation, LLC (“PWR”). My primary business address is 1710 Woodcreek Farms Road, Elgin, SC 29045. Ni is owned by Pacolet Milliken, LLC, a South Carolina company owned principally by the Milliken family (“Pacolet”).

Q. WHAT IS YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND?

A. I graduated from Westminster College in New Wilmington, Pennsylvania, with a Bachelor of Arts degree and the University of Miami with a Master of Business Administration degree. I have over 15 years of water and wastewater experience and have worked in the utility industry for over 23 years. My complete work history prior to beginning work with Ni and its predecessors is set forth on Appendix A to my testimony.

1 In 2010, I joined Ni America Capital Management, LLC and thereafter joined Ni. Prior to
2 becoming its President, I served and continue to serve as Ni's Chief Financial Officer.
3

4 **Q. WHAT ARE YOUR DUTIES IN YOUR CURRENT POSITION?**

5 A. As Chief Financial Officer of Ni, I am ultimately responsible for all financial issues,
6 and day-to-day financial operations of six utility systems representing over 45,000
7 equivalent residential connections in South Carolina and Florida. As Chief Financial
8 Officer of PWR, my responsibilities include the day-to-day oversight of all financial,
9 accounting, customer billing and relations, and banking and rates functions. In the event
10 that a customer complaint or dispute is not resolved by the Supervisor or Manager of
11 Customer relations, I speak directly with customers in an effort to resolve their concerns.
12

13 **Q. HAVE YOU HAD ANY INVOLVEMENT IN OTHER RATE/REGULATORY**
14 **PROCEEDINGS?**

15 A. I have been involved in numerous rate proceedings and settlement negotiations in
16 a number of states, including the Commonwealth of Pennsylvania's electric utility
17 deregulation proceedings where, among other duties, I was responsible for Duquesne
18 Light's cost of capital testimony, its testimony related to the proposed two hundred mile
19 long Duquesne Light to General Public Utilities Transmission Line, fuel clause adjustment
20 filings, and general rate filings for utilities in Texas, Florida, and South Carolina. I was
21 recently a witness in the rate case in Commission Docket Number 2017-228-S, which
22 involved Palmetto Utilities, Inc., also an indirect subsidiary of Pacolet.
23

24 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

25 A. The purpose of my testimony is to (1) provide the Commission with an overview
26 of the financial structure of Ni America Operating, LLC (a sister company of Ni) and the
27 allocation of overhead, (2) review background issues and specific financial issues related
28 to PWR, its rates and rate application, and (3) generally support PWR's need for rate relief.

1 **Q. WHAT IS THE BACKGROUND OF PWR AND ITS OWNERSHIP?**

2 A. As the Commission is aware, Alpine Utilities, Inc. and Woodland Utilities, Inc.
3 were separate public utility companies which began operating in the midlands area in the
4 late 1960s and early 1970's. In August 2011, they were transferred to PWR with the
5 Commission's approval under Order Number 2011-320 in Docket Number 2011-65-S. In
6 a rate case filed in 2014, specifically in Commission Docket Number 2014-69-S, the Alpine
7 and Woodland systems were consolidated and their rate schedules were merged creating a
8 uniform rate for all customers.
9

10 **Q. WHAT IS NI'S AND PWR'S COMMITMENT TO REGULATORY AND**
11 **ENVIROMENTAL COMPLIANCE, AND HOW HAVE THEY DEMONSTRATED THAT**
12 **COMMITMENT?**

13 A. Ni America was founded in April 2007 to acquire small to mid-sized water and
14 wastewater companies. The members of the management team of Ni pride themselves on
15 having the reputation and dedication to bring undercapitalized utility systems into
16 regulatory and environmental compliance and striving to achieve best industry practices in
17 operations. PWR acquired the assets of Alpine Utilities, Inc. and Woodland Utilities, Inc.,
18 which were undercapitalized systems plagued with numerous Sanitary Sewer Overflows,
19 or "SSOs," and desperately in need of plant upgrades and cleaning and repair of their
20 collection systems. Before purchasing the utilities, PWR at its request entered into a
21 Memorandum of Understanding, or "MOU," with the South Carolina Department of Health
22 and Environmental Control, or "DHEC," to make needed improvements and repairs over
23 a five-year period to the Alpine wastewater treatment facilities and the Alpine and
24 Woodlands collection systems. Mr. Bryan Stone, Ni's Chief Operating Officer will discuss
25 the work performed in this regard in more detail in his testimony.

26 In summary, since the last rate relief proceeding for PWR, we have spent
27 approximately \$6.8 million on the improvements and repairs to these systems as agreed
28 upon in the MOU and we have provided documentation to DHEC as to our progress. The
29 total investments that we have made in PWR since we entered into the MOU now exceeds

1 \$13 Million. Work under the MOU is now complete and has been accepted by DHEC as
2 meeting the obligations of the MOU. This project and our continuing efforts strongly
3 reflect our commitment to achieving exemplary environmental quality performance
4 standards.
5

6 **Q. WHAT HAS BEEN THE BENEFIT OF THE CAPITAL SPENDING UNDER THE MOU**
7 **PROJECT AND THE OTHER CAPITAL SPENDING?**

8 A. Ni, through PWR's purchase of these two utilities and the further investments by
9 PWR, took two troubled systems that had a significant number of SSO's and completely
10 refurbished the systems. Both systems now operate at a high standard and have very few
11 SSO's. This was accomplished while at the same time keeping rates to customers relatively
12 low as shown in the chart attached to my testimony as MD Exhibit 1. The acquisitions and
13 subsequent refurbishments are an excellent example of a privately-owned utility bringing
14 private capital into the industry and working with DHEC to eliminate a compliance
15 problem for the State of South Carolina. As a matter of good public policy, the
16 Commission's approval of asset transfers and public utility consolidations encourages this
17 type of action by a utility. Recovery of the necessary investments to make such
18 acquisitions, improvements, and consolidations happen is the key to this policy. Ni hopes
19 to find other utilities in the state where its expertise and capital can be brought to bear on
20 refurbishing systems in need of it. Earning a fair return on such investments is vital.
21

22 **Q. YOU PREVIOUSLY MENTIONED NI AMERICA OPERATING, LLC; WHAT IS ITS**
23 **RELATIONSHIP TO PWR?**

24 A. Ni America Operating, LLC ("Ni America Operating") is a service company that
25 contains the employees that serve the utilities owned by Ni. Therefore, its financial books
26 reflect the costs for the overhead and "shared services". The shared services performed by
27 Ni America Operating include accounting, customer service, billing, finance and cash
28 management, third party operator contract management, capital project management, and
29 engineering. Ni America Operating has 32 employees with management having over 100

1 combined years of water and wastewater experience. These employees include engineers,
2 CPA's, administrative personnel and field personnel. The management of Ni America
3 Operating prides itself on its reputation and its dedication to constantly improving the
4 standards of operations, regulatory compliance and customer service in a cost-effective
5 manner.
6

7 **Q. WOULD YOU PLEASE EXPLAIN THE OVERHEAD ALLOCATION PROCESS**
8 **PERTINENT TO THIS PROCEEDING?**

9 A. For rate case purposes, all applicable corporate overhead costs are either allocated
10 or specifically assigned to the utilities. The companies where corporate overhead costs are
11 incurred are 1) Ni America Operating and 2) Pacolet. As noted above, Pacolet owns Ni
12 and all of its affiliates. The corporate overhead costs (1) may be allocated based on
13 Equivalent Residential Connections ("ERCs") for all utilities, or (2) may be specifically
14 assigned to the utility that receives the benefit of the cost incurred.

15 The largest contributor to corporate overhead costs is Ni America Operating, whose
16 related costs include payroll, benefits, office rent and expenses, and travel. Pacolet
17 contributes some corporate overhead costs and includes costs for employees doing work
18 that benefits Ni's utilities, including costs for their corporate financing and governance, as
19 well as direct support on contractual, construction and regulatory matters. The percentage
20 of time/expense of Pacolet employees allocated to Ni ranges from 5% to 50%. In preparing
21 the rate filing, certain costs recorded for Ni America Operating are excluded from the
22 allocation due to one of the following reasons: they have been disallowed by the
23 Commission in previous rate filings, they are specifically assignable to a particular utility,
24 or they are for activities that do not benefit the utility customers. These include such items
25 as bonuses, severance, and due diligence expenses. After all of these costs are excluded,
26 the remaining costs are allocated to the utilities based on the ratio of PWR's ERCs to the
27 total ERCs managed by Ni America Operating.

28 Then, there are some expenses for Ni America Operating which may be incurred
29 for a specific utility. An example of this would be the direct allocation of an invoice for a
30 service provided to one but not both of the South Carolina utilities owned by Ni. As such,

1 these expenses are removed from the allocation in #1 above, and specifically assigned to
2 the utility receiving the benefit for this cost.

3 By sharing the overhead and management employees between the two utilities in
4 South Carolina, which comprise four systems and over 45,000 ERCs, duplication of costs
5 is eliminated, and efficiencies are captured which benefit our customers.

6 **Q. DOES PWR USE ITS OWN PERSONNEL TO OPERATE THE SYSTEMS?**

7 A. No. It uses a third- party contract operator for that function. PWR has both the
8 technical and financial expertise in-house to manage its third- party operator. However,
9 Ni America Operating has four employees who are 100% dedicated to the underground
10 refurbishment capital projects and whose expense is allocated between all utility systems.
11

12 **Q. HOW DOES THE USE OF A THIRD-PARTY OPERATOR BENEFIT CUSTOMERS?**

13 A. Ni's goal is to operate every utility system in a manner as close to industry best
14 practices as is reasonably practical for the size of the system and with due consideration of
15 the related cost to the customer. We find that using an independent third-party operator
16 and engaging them on a fixed cost basis allows us to better control operating costs and keep
17 overhead down. This allows us to transfer some of the risk of the day-to-day uncertainty
18 of operations to the third-party operator. While the cost of the third-party operator
19 increases annually, the increase is based on a formula tied to a specific inflation factor.
20 Also, Ni can leverage the third-party operator's existing economies of scale to provide our
21 customers with additional services, such as enhanced environmental and safety compliance
22 at a more effective cost. These contracts have a five-year term, but they are cancellable
23 upon ninety days' notice. This allows Ni to demand high operating standards without the
24 associated risk and cost of replacing underperforming company employees (if Ni
25 performed this function in-house). Also, these contracts are competitively bid among
26 several service providers, which ensures that costs are kept down. This compares favorably
27 with bringing people in-house as direct employees. While it is difficult to get comparable
28 industry data, PWR believes that its cost of operations (including overhead) is lower than
29 most other similarly-sized utilities.
30

1 **Q WHEN WAS THE LAST GENERAL RATE INCREASE REQUESTED FOR**
2 **CUSTOMERS OF PWR?**

3 A. PWR last requested a general rate increase in March of 2014, based on a test year
4 ending December 31, 2013. By Order Number 2014-752 in Docket Number 2014-69-S,
5 the Commission authorized an increase to \$34.50 per single family equivalent, or “SFE,”
6 effective September 18, 2014.
7

8 **Q. IS PWR IN NEED OF CURRENT RATE RELIEF?**

9 A. Yes. As the financial statements attached as exhibits and schedules to this
10 Application demonstrate, and as the testimony of PWR witness Donald Clayton confirms,
11 PWR is earning below its previously authorized operating margin. This is due primarily
12 to capital expenditures made and, to a lesser extent, increases in its operational expenses
13 and loss of customers since its last rate relief proceeding.
14

15 **Q. WHAT HAS BEEN THE CUSTOMER GROWTH AT PWR SINCE THE LAST RATE**
16 **CASE?**

17 A. Unfortunately, there has been no growth, but a decrease in customers. The number
18 of SFEs today are approximately 630 less than in our last rate filing. This is a concern as
19 new customer growth greatly helps existing customers in that it increases the number of
20 available customers over which the cost of service and revenue requirement may be spread,
21 while customer loss does the opposite. Some of the decrease was due to the loss of an
22 apartment complex due to the flood of 2015. Other losses were due to commercial
23 customers closing down. Ms. Andrena-Powell-Baker’s testimony outlines some steps
24 PWR will take to try to bring more customers into the service territory.
25

26 **Q. WHAT HAS BEEN PWR’S OPERATING (O&M) EXPERIENCE SINCE THE LAST**
27 **RATE CASE?**

1 A. Since the last rate filing, annual Operations and Maintenance expense (not
2 including property taxes) has increased \$64,000. This equates to an average annual
3 increase of roughly 1.5% per year, lower than the rate of inflation.
4

5 **Q. WHAT IS THE EFFECT OF THE \$6.8 MILLION IN NEW CAPITAL EXPENDITURES**
6 **DISCUSSED HERE AND IN MR. STONE'S TESTIMONY ON PROPERTY TAXES?**

7 A. Property taxes for utilities assessed by the South Carolina Department of Revenue
8 and paid to Lexington County are based on net book value. The \$6.8 million in capital
9 expenditures will increase net book value by that amount. Unfortunately, this will increase
10 property taxes by approximately \$376,000 per year.
11

12 **Q. HOW DO PWR'S RATES COMPARE TO THE SEWER RATES OF OTHER**
13 **NEIGHBORING UTILITIES?**

14 A. My MD Exhibit 1 shows the neighboring residential sewer utility rates and the
15 proposed increased PWR rate. The information in this table was part of the presentation
16 given at the three town hall meetings described in Ms. Powell-Baker's testimony. PWR's
17 customers have benefitted from its low rates for many years, and even after the capital
18 spent for the major refurbishments discussed above and the resulting requested increase,
19 our customers' rates are still much lower than most neighboring sewer utilities. This is
20 despite being significantly disadvantaged by the fact that most of our neighboring utilities
21 are government-owned and do not pay property and income taxes as we do. PWR expects
22 to have a relatively flat rate growth trajectory for many years and therefore fully expects to
23 stay at the lower end of the price spectrum.
24

25 **Q. ARE THE RATES AND CHARGES PROPOSED FAIR, REASONABLE, AND**
26 **NECESSARY IN ORDER FOR PWR TO CONTINUE TO PROVIDE SAFE AND**
27 **RELIABLE WASTEWATER TREATMENT SERVICE?**

1 A. Yes. The financial statements and the testimony of Mr. Clayton clearly reflect the
2 financial position of PWR. In order to continue to provide the type of services which we
3 have been providing, PWR must have rate relief. PWR believes that the proposed rates
4 fairly distribute the cost to the consumer for providing those services, while at the same
5 time placing the utility on more solid financial footing. This will allow PWR to attract
6 additional capital to continue financing operations and fund any needed future capital
7 expenditures. PWR is committed to continuing to provide quality service in an
8 environmentally responsible manner. It is our belief that the rates requested are reasonable,
9 fair, responsible, non-discriminatory and justified in light of the customer responsibilities,
10 PWR's requirements to meet the customers' needs, and its commitment to do so in
11 compliance with regulations of this Commission, DHEC, and other regulatory agencies.
12

13 **Q. IS PWR REQUESTING THAT ITS RATES BE SET IN THIS PROCEEDING USING THE**
14 **RETURN ON RATE BASE METHODOLOGY?**

15 A. Yes. The substantial investment in rate base by PWR of approximately \$10.6
16 million warrants a rate of return methodology instead of an operating margin methodology.
17 As this Commission has previously observed, the return on rate base methodology is
18 warranted where a utility has a large rate base and needs to earn a rate of return sufficient
19 to obtain the necessary equity and debt capital that a larger utility needs for sound
20 operation. Although the Commission is required to state the resultant operating margin
21 after it determines just and reasonable rates, it should not use operating margin as a guide
22 to set rates where the circumstances justify use of the rate of return method. Given PWR's
23 substantial rate base and its need to earn a fair and reasonable rate of return on its
24 investment, a rate of return on rate base methodology is the appropriate rate-setting
25 methodology to use in this case.
26

27 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

28 A. Yes, it does.

APPENDIX A TO DIRECT TESTIMONY OF MARK S. DADAY

1985 to 1989	Employed by GATX-Fuller Company, a multi-national manufacturing firm, in various financial roles.
1989 to 2003	Duquesne Light Company, the electric utility serving Pittsburgh, Pennsylvania, and its affiliates. Duquesne was a publicly-traded company listed on the New York Stock Exchange at the time, with over 600,000 customers and \$1.1 billion in revenue. I held various positions in the financial group, including Assistant Treasurer, an officer level position.
1998	Founding board member of AquaSource, a water and wastewater utility and an affiliated company of Duquesne. AquaSource was involved in over 80 acquisitions and eventually grew to \$200 million in annual revenue.
1998	Chief Financial Officer of another company affiliated with Duquesne, DQE Systems, and subsequently served as its President. DQE Systems operated a propane gas distribution company and a fiber optic network company in Pittsburgh. In these roles at DQE Systems, I maintained my involvement with Duquesne Light Company, including serving on its pension investment management committee.

MD EXHIBIT 1
Neighboring Monthly Residential Wastewater Rates

	Current
Town of Winnsboro ^{(1) (2)}	\$72.89
Town of Lexington ⁽²⁾	\$68.84
City of Columbia ^{(1) (2) *}	\$66.58
Carolina Water	\$65.09
City of Cayce ⁽²⁾	\$54.38
Palmetto Utilities	\$52.10
City of Columbia (in city rates) ^{(1) *}	\$51.64
Lexington County Joint Municipal ⁽¹⁾	\$51.33
Richland County – Broad River	\$44.54
Midlands/DSI (Synergy)	\$43.00
Palmetto Wastewater Reclamation	\$41.18
Kershaw County ^{(1) (4)}	\$40.00
East Richland County PS District ⁽³⁾	\$35.77

* Recently filed a notice of intent to raise rates. Rates expected to rise significantly over the next 5 years due to \$750 million consent decree with EPA

Notes:

- (1) Assumes 6,000 gal. per month
- (2) Out of city rates
- (3) Includes estimate of ad valorem tax subsidies
- (4) Does not include the impact of any tax revenues used to support wastewater system.